

MEDIA RELEASE



11 December 2013

FONTERRA MAINTAINS FORECAST FARMGATE MILK PRICE FOR 2013/14 SEASON AND CONTINUES INVESTING IN THE FUTURE

Forecast

Fonterra Co-operative Group Limited is maintaining its forecast Farmgate Milk Price for the 2013/14 season at \$8.30 per kgMS.

Chairman John Wilson said milk powders are continuing to sell at very high prices because of the strong global demand and limited supply.

“Only four months into the season, we are in an extraordinary situation.

“The gap between prices for milk powders compared to cheese and casein is greater than it has ever been before.

“The high powder prices are good for our farmer shareholders, and good for New Zealand.

“The forecast Farmgate Milk Price, which is calculated under the Milk Price Manual, is based on processing and manufacturing milk powders. The calculation is also based on the costs involved in production for an efficient manufacturer of Fonterra’s size and scale.

“However, Fonterra’s actual asset base includes a number of cheese and casein manufacturing plants which means that we are not able to maximise profits from these plants in the current environment.

“In such abnormal circumstances, the Board has the discretion to pay a lower Farmgate Milk Price than that specified under the Manual, if it is in the best interests of the Co-operative.

“Today’s forecast is our best estimate, but given the current volatility it may change over the course of the season. As a result of this volatility, the Board has also lowered the dividend forecast for the 2014 financial year to 10 cents per share,” said Mr Wilson.

CEO Theo Spierings said “Doing nothing, and forecasting a Farmgate Milk Price that is higher than we can afford to pay at this stage in the season, is not an option.

“We will maintain our financial discipline and not pay the Milk Price out of borrowings – particularly in a year when we are forecasting a record payout for our farmers.”

Fonterra is required to consider its Farmgate Milk Price every quarter as a condition of the Dairy Industry Restructuring Act (DIRA).

For personal use only

Following the Board's decisions, today Fonterra is announcing that:

- The Farmgate Milk Price will be maintained at its current level of \$8.30 per kgMS;
- This is 70 cents per kgMS below the theoretical Farmgate Milk Price of \$9.00 per kgMS calculated in accordance with the Milk Price Manual;
- The estimated full year dividend will be 10 cents per share - delivering a forecast Cash Payout of \$8.40;
- Forecast EBIT (Earnings Before Interest and Tax) for the financial year ending 31 July 2014 is currently estimated at \$500-\$600 million.

The Board has also approved an increase in the Advance Rate schedule of monthly payments to farmer shareholders. The December payment, paid in January 2014, will be increased by 30 cents to \$5.80.

Impact of the global situation on stream returns and the forecast Farmgate Milk Price

Fonterra processes its milk into two main product groups – powders (whole milk powder and skim milk powder) and other products (including cheese, casein, milk protein concentrate, nutritionals, and liquid milk). These product groups are referred to as “streams”.

Mr Spierings said “This season, we have devoted the maximum possible volume of milk to whole milk powder and skim milk powder streams to maximise payments to our farmers. However, we have not been able to lift powder production above the current 70 per cent level as we are limited by the nature of Fonterra's existing production facilities in New Zealand.

“That is why the remaining 30 per cent of milk is being converted to cheese and casein which are currently generating lower returns.

“The current strong prices for milk powder are being driven by increasing levels of demand from China, and emerging economies in Asia and North Africa.

“Meanwhile, domestic factors in key markets such as Europe, the United States and Japan mean cheese and casein prices are not keeping pace with powders. These factors include local milk pricing regulations, trends in local demand for cheese, and trade barriers.

“Since Fonterra was formed, we have not invested in any new cheese or casein plants and have been evolving our manufacturing asset base to invest in additional milk powder production facilities. Last weekend we officially opened the world's largest powder drier at Darfield in Canterbury,” said Mr Spierings.

Mr Wilson said that the Board has approved \$235 million for the development of a third powder drier at Pahiatua in the lower North Island.

“We anticipated that the market would likely change and that demand for milk powders would increase – but the demand is increasing at a faster rate than anyone predicted.

“Today's forecast Farmgate Milk Price ensures the Co-operative can stay on course with its strategy and continue optimising the value of our New Zealand milk,” said Mr Wilson.

Staying on strategy and investing in the future

Volatility has become the new norm, and Fonterra must have the flexibility to respond quickly to shifting global demands for dairy nutrition, said Mr Spierings.

“We need to continue investing in greater flexibility in our manufacturing assets so we can meet changes in global demand and commodity cycles.

For personal use only

“The new market realities mean new opportunities – and we must go after them now as we have in the past by driving forward with our volume and value strategy.

“We are already doing this. Along with the approval of the new drier at Pahiatua, work is well underway on our new UHT plant at Waitoa and the new drier at Darfield has already produced more than 50,000 metric tonnes of whole milk powder since it was commissioned at the beginning of the season.

“We have also recently made significant investments to expand our global foodservice capabilities. These include doubling the capacity of our Clandeboye plant to produce individual quick frozen (IQF) grated mozzarella, and expanding our cream cheese plant at Te Rapa. The foodservice category includes full and quick service restaurants, institutions, hotels, airline catering facilities and other commercial kitchens.

“Over the next few months we will look at additional measures that will further improve our ability to provide higher volumes of the dairy commodities global customers want – when they want them,” said Mr Spierings.

Further information relating to this announcement is available on Fonterra.com.

- ENDS -

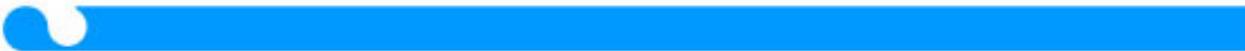
For further information contact:

Fonterra Communications
Phone: +64 21 507 072

About Fonterra

Fonterra is a global leader in dairy nutrition – the preferred supplier of [dairy ingredients](#) to many of the world's leading food companies. Fonterra is also a market leader with our own [consumer dairy brands](#) in Australia/New Zealand, Asia/Africa, Middle East and Latin America.

The [farmer-owned](#) New Zealand co-operative is the largest processor of milk in the world, producing more than two million tonnes of dairy ingredients, value added dairy ingredients, specialty ingredients and consumer products every year. Drawing on [generations of dairy expertise](#), Fonterra is one of the largest investors in dairy based [research and innovation](#) in the world. Our more than [16,000 staff](#) work across the dairy spectrum from advising farmers on sustainable farming and milk production, to ensuring we live up to exacting quality standards and delivering every day on our customer promise in more than 100 markets around the world.



If this material is not relevant to your purpose, you may wish to prevent further deliveries via email. To opt-out, please [click here](#)

For personal use only

FONTERRA:

- Global Outlook
- Farmgate Milk Price Forecast
- A Year in Review

11 December 2013

© FONTERRA CO-OPERATIVE GROUP LIMITED



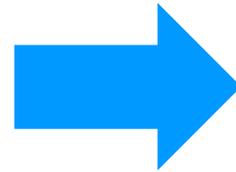
Dairy for life

Contents

1. The global dairy market
2. How we set the Farmgate Milk Price
3. The widening price gap between milk powders and other dairy products
4. Managing our product mix
5. Continuing to invest in our strategy
6. Building a stronger Co-operative

The global dairy market is changing

Tight supply
and strong
demand for
milk powder



Record global
dairy prices

***Extraordinary events are having both a positive
and negative impact on Fonterra***

Fonterra processes milk into a variety of 'streams'

For personal use only



Main Products

Whole Milk Powder (WMP)

Skim Milk Powder (SMP)

By-products

Butter

Anhydrous Milk Fat (AMF)

Buttermilk Powder (BMP)

WMP stream

SMP stream



Cheese

Casein

Other

Whey Protein

Butter/BMP

Lactose

Other

Cheese stream

Casein stream

Other streams

The main products and their by-products are referred to as 'streams'

How we set the Farmgate Milk Price

POWDER PRODUCTS



70%



30%

OTHER PRODUCTS
(Cheese, Casein etc.)



Used to calculate
Farmgate Milk Price as per
Milk Price Manual

\$9.00

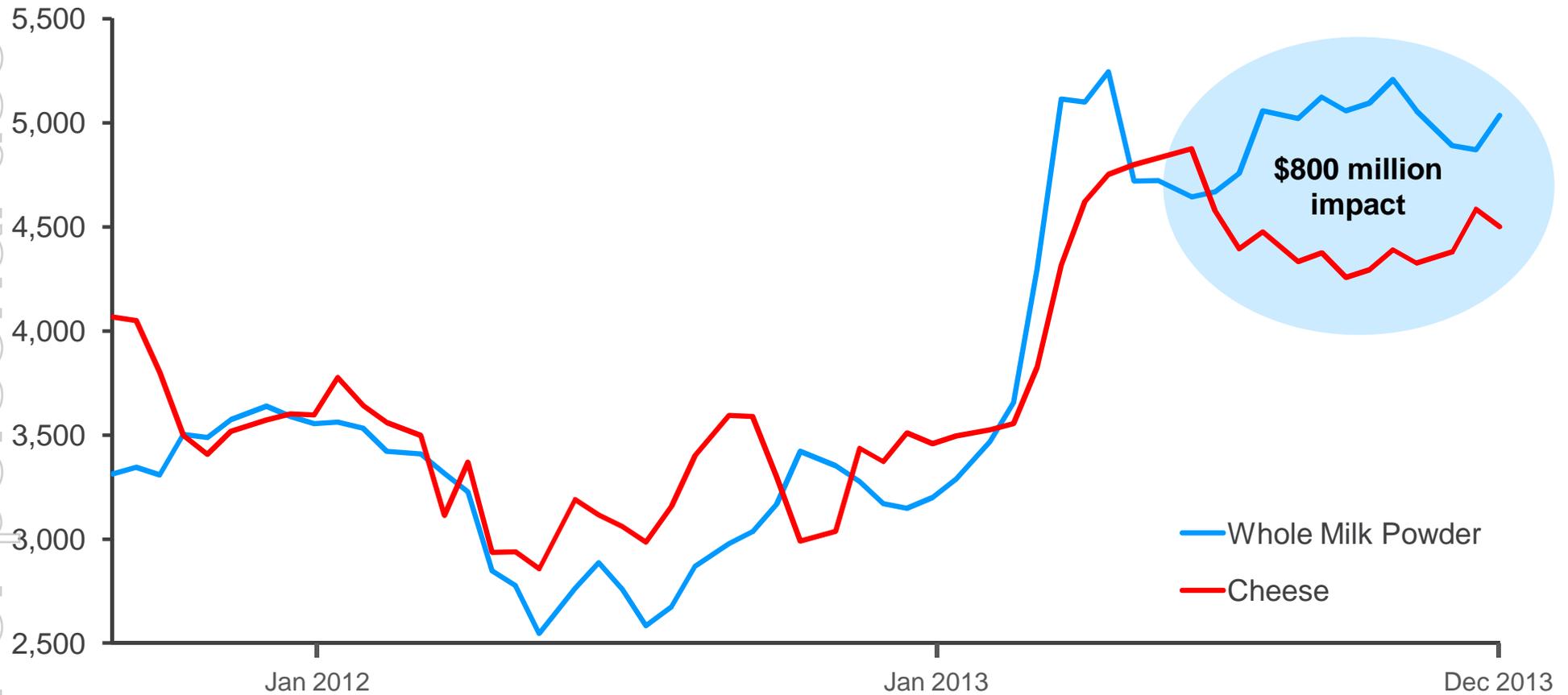
The Farmgate Milk Price
is applied to all products



For personal use only

The prices have widened between milk powder and other dairy products

US\$ per MT



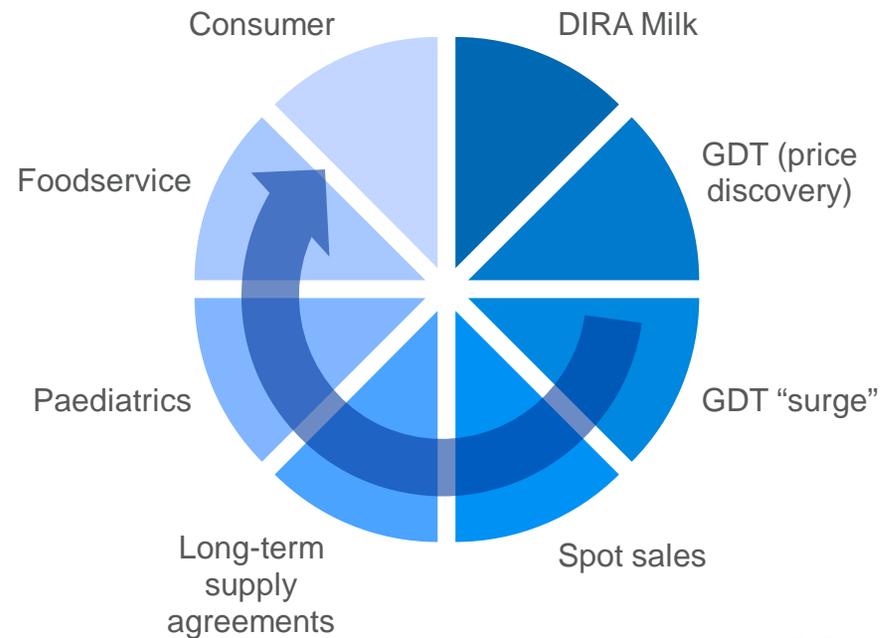
For personal use only

Continuing to invest in our strategy

For personal use only

- 1 World-class manufacturing plants in New Zealand
- 2 Global Foodservice
- 3 UHT and infant formula in China
- 4 Strong consumer brands in Asia and Latin America
- 5 Australia turnaround
- 6 Investment in global milk pools

'Turning the Wheel'



A big year for the Co-operative

For personal use only



**WORST DROUGHT
IN 70 YEARS**



DCD



**FOODSERVICE
EXPANSION**



**WPC80
PRECAUTIONARY
RECALL**



**RECORD MILK
FLOWS**



**WORLD'S
LARGEST
MILK
DRYER**



**INFANT
FORMULA
IN CHINA**



**ANCHOR
UHT LAUNCHED
IN CHINA**



PAHIATUA